

COUNTY OF YUBA
MANAGEMENT REPORT
FOR THE YEAR ENDED
JUNE 30, 2008

Mgt. Ltr.
3/23/09

COUNTY OF YUBA

Management Report For the Year Ended June 30, 2008

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BARTIG, BASLER & RAY, LLP

A GALLINA LLP COMPANY

CERTIFIED PUBLIC ACCOUNTANTS

To the Honorable Board of Supervisors
County of Yuba
Marysville, California

In planning and performing our audit of the basic financial statements of the County of Yuba (County) as of and for the year ended June 30, 2008, in accordance with auditing standards generally accepted in the United States of America, we considered the County's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the County's internal control. Accordingly, we do not express an opinion on the effectiveness of the County's internal control.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or a combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or a combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of internal control was for the limited purpose described in the first paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. In addition, because of inherent limitations in internal control, including the possibility of management override of controls, misstatements due to error or fraud may occur and not be detected by such controls. We consider the following deficiencies to be significant deficiencies or material weaknesses in internal controls as reported within the Schedule of Findings and Questioned Costs of the Single Audit report:

- Finding 07-FS-1: Material Weakness: Trust Funds.
- Finding 07-FS-2: Material Weakness: Construction in Process.
- Finding 07-FS-3: Material Weakness: Infrastructure Accounting and Depreciation
- Finding 07-FS-4: Material Weakness: Financial Reporting Competencies
- Finding 08-FS-1: Material Weakness: Accounting for Capital Leases
- Finding 08-FS-2: Significant Deficiency: Escrow Accounts Outside the Treasury
- Finding 08-FS-3: Material Weakness: Capital Contributions
- Finding 08-FS-4: Material Weakness: Receivables

We previously reported on the County's internal control in our report dated February 6, 2009. A separate report dated February 6, 2009, contains our report on the significant deficiencies and material weaknesses in the County's internal control and identified above. This letter does not affect our report dated February 6, 2009, on the financial statements of the County of Yuba.

However, during our audit we became aware of several matters that are opportunities for strengthening internal controls and operating efficiency. The memorandum that accompanies this letter summarizes our comments and suggestions concerning those matters.

This report is intended for the use of management, the Board of Supervisors, management and officials of the federal and state grantor agencies.

We thank the County's staff for its cooperation during our audit.

BARTIG, BASLER & RAY, LLP
A GALLINA LLP Company

Bartig, Basler & Ray, LLP

Roseville, California
February 6, 2009

COUNTY OF YUBA

Management Report Required Communication For the Year Ended June 30, 2008

The Auditor's Responsibility under U.S. Generally Accepted Auditing Standards and OMB Circular A-133

As stated in our engagement letter dated June 10, 2008, our responsibility, as described by professional standards, is to plan and perform our audit to obtain reasonable, but not absolute assurance that the financial statements are free of material misstatement and are fairly presented in accordance with U.S. generally accepted accounting principles. Because an audit is designed to provide reasonable, but not absolute assurance and because we did not perform a detailed examination of all transactions, there is a risk that material misstatements may exist and not be detected by us.

In planning and performing our audit, we considered the County's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide assurance on the internal control over financial reporting. We also considered internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

As part of obtaining reasonable assurance about whether the County's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit. Also, in accordance with OMB Circular A-133, we examined, on a test basis, evidence about the County's compliance with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement applicable to each of its major federal programs for the purpose of expressing an opinion on the County's compliance with those requirements. While our audit provides a reasonable basis for our opinion, it does not provide a legal determination on the County's compliance with those requirements.

Planned Scope and Timing of the Audit

We performed the audit according to the planned scope and timing previously communicated to you in our engagement letter dated June 10, 2008.

COUNTY OF YUBA

Management Report Required Communication For the Year Ended June 30, 2008

Qualitative Aspects of Accounting Practices

Significant Accounting Policies

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the County are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the year ended June 30, 2008. We noted no transactions entered into by the County during the year for which there is a lack of authoritative guidance or consensus. There are no significant transactions that have been recognized in the financial statements in a different period than when the transaction occurred.

Significant Accounting Estimates

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimate(s) affecting the financial statements were:

- Accrual and disclosure of compensated absences
- Capital asset lives and depreciation expense
- Allowance for uncollectible accounts
- Actuarial valuations of risk management liability

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit other than those that are trivial, and communicate them to the appropriate level of management.

COUNTY OF YUBA

Management Report Required Communication For the Year Ended June 30, 2008

Material Misstatements Corrected by Management

The following material misstatements that we identified as a result of our audit procedures were brought to the attention of, and corrected by, management:

- Receivables were understated by \$806 thousand. The County received the funds after its year-end closing cut-off date for analyzing general ledger transactions for possible accruals.
- Several significant adjustments were made to capital asset account balances, including \$37.8 million to account for new capital lease on building, \$1.8 million to account for capital contributions of land and \$3.3 million to account for road construction costs.
- Accounting standards require the financial statements include a liability representing the estimated amount of claims likely to exist against the County's self-insurance program. An actuarial study determined the amount to be \$1.1 million at June 30, 2008. This liability was not recorded on the County's general ledger.
- The County holds cash and investments with an external fiscal agent for the purpose of meeting reserve provisions in its existing debt agreement and for facilitating the semi-annual principal and interest payments. The balance at June 30, 2008 was \$303 thousand. This amount was not recorded on the County's general ledger.
- The County was holding \$332 thousand with an external fiscal agent to fund its retention owed to contractors for a road project. This amount was not recorded on the County's general ledger.

Material Misstatements Not Corrected by Management

The County has omitted the financial statements of the Yuba County Water Agency (the Agency), which statements reflect total assets of \$227,132,315 as of June 30, 2008, and total revenues of \$26,189,690 for the year then ended. The Agency should be included with the County under Government Accounting Standards Board (GASB) Statement No. 14, *The Financial Reporting Entity*, as amended by GASB No. 39, *Determining Whether Certain Organizations are Component Units* because the Agency is a legally separate entity with substantively the same governing board as the County. Of the seven board members that govern the Agency, five of those members serve as the County's Board of Supervisors. In our opinion, disclosure of that information is required to conform with accounting principles generally accepted in the United States of America.

Because of the inadequacy of accounting records for the contributed infrastructure for the years prior to 2008, we were unable to form an opinion regarding the amounts at which infrastructure and the related accumulated depreciation are recorded in the Statement of Net Assets for Governmental Activities at June 30, 2008 (stated at \$189,701,979 and \$77,805,805), respectively, and the amount of depreciation expense related to infrastructure for the year then ended (stated at \$7,346,918).

Immaterial Misstatements Not Corrected by Management

COUNTY OF YUBA

Management Report – Current Year Comments For the Year June 30, 2008

YEAR END CLOSING PROCEDURES

Condition

The County's general ledger is maintained on essentially a cash basis throughout the year. Account balances for receivables, payables, expense accruals and capital assets are determined on an annual basis and journal entries are posted to a period 13 in the County's accounting system. Information for receivables and payables is collected by the Auditor-Controller's office by looking at transactions that occur in July and the early part of August. Except for larger departments, such as, Health and Human Services and the Sheriff, this information is determined independent of other department participation.

During our audit, we noted that the subsequent transactions (July and August deposits and disbursements) do not provide enough information to accurately record all adjustments necessary to convert the County's general ledger to a basis which conforms with existing reporting standards. In those cases where participation from departments was solicited, information was not provided soon enough so that adjustments could be posted before the books were closed.

Effect of Condition

An inaccurate and incomplete closing process results in audit adjustments. Statement on Auditing Standards No. 112 requires the auditor to consider material audit adjustments as at least a significant deficiency and a strong indicator of a material weakness in internal control over financial reporting. A closing process that involves input from others and adheres to a well-documented process having assigned responsibilities and due dates results in accurate and complete account balances.

Recommendation

We recommend the closing process be documented in a checklist that indicates who will perform each procedure and when completion of each procedure is due. Consideration should be given to having departments submit receivable and payable information to the Auditor-Controller's office using a standardized form requiring departments to attach appropriate documentation and support. Departments should be trained so that they will understand the accounting terms used and the nature of the information being requested. Due dates should be established, communicated and monitored.

COUNTY OF YUBA

Management Report – Current Year Comments For the Year June 30, 2008

JOURNAL ENTRY PROCESS

Condition

Journal entries are prepared by the Auditor-Controller's office often in response to requests received from departments. These responses come in many different forms. Many are emails sent by County department personnel requesting some change or correction in an account balance or transaction. Some are memos or notes dropped off at the Auditor-Controller's office. In other cases, journal entries are recorded solely at the discretion of the personnel in the Auditor-Controller's office.

We also observed that although a standardized journal entry form is often used by the Auditor-Controller's office, it is not always used. Some journal entries occur with routine frequency indicating opportunities for use of pre-formatted recurring journal entry documentation.

Effect of Condition

Journal entries which are prepared by the Auditor-Controller's office on behalf and at the request of departments use Auditor-Controller staff resources that could be better utilized elsewhere. Departments are held more accountable for the accuracy of their financial accounts when they are also responsible for preparing corrections using a standard journal entry form which is authorized by department supervisors and submitted to the Auditor-Controller's office for approval and posting.

Corrections which are made by the Auditor-Controller's office in response to a department request may lack proper approval from departmental supervisors whose accounts are being adjusted.

Recommendation

We recommend the County implement the use of a standard journal entry form, available in electronic format and requiring all department personnel to complete it in cases where corrections to accounts are required. The form should prompt for the attachment and inclusion of appropriate explanation and support. The form should be approved by the appropriate departmental supervisors before submitting it to the Auditor-Controller's Office. The Auditor-Controller's Office should be responsible for reviewing the accuracy of the adjustment(s) before posting it to the County's general ledger.

COUNTY OF YUBA

Management Report – Current Year Comments For the Year June 30, 2008

CENTRALIZED PURCHASING SYSTEM

Condition

Although the Administrative Department is considered the purchasing agent for the County and this department has responsibilities for bidding processes and contracts, the County does not use a centralized purchasing system. There is no approved vendor list. Purchase requisitions and purchase orders are not routinely used.

Appropriation limits are the responsibility of each of the departments. Departments must keep track of their budgets and the remaining unspent appropriations before making additional purchase commitments. The County's current process is detective and not preventive as it is only capable of identifying situations where overspending has occurred. It does not prevent users from overspending. Each department initiates their own purchases according to the County purchasing policy with department head authorization.

Effect of Condition

A centralized system of purchasing enhances internal controls by the use of requisition forms or purchase orders to prevent overspending and to ensure the County pays only for items or services that are actually received. A centralized system of purchasing also results in cost savings because of standardized pricing, consolidation of the vendor list and volume pricing.

Recommendation

We recommend the County explore the capabilities of its current accounting system to determine if implementing a centralized purchasing module or system is feasible. If determined to be possible, the County should consider the staffing needs and changes in procedures required for successful implementation.

COUNTY OF YUBA

Management Report – Current Year Comments For the Year June 30, 2008

REVIEW OF PAYROLL INPUT PRIOR TO PROCESSING PAYCHECKS

Condition

Payroll is input by accounting staff in the Auditor-Controller's office using the payroll vendor's software and interface and timesheet summaries submitted by departments. After input, the accounting staff review the data input to ensure it is correct before transmitting the information to the payroll vendor for processing. There is no independent review of the payroll function prior to transmitting the data to the payroll vendor.

Effect of Condition

Internal controls that help prevent and detect errors or misappropriations are improved when the review of the data input is performed by someone outside of the data input process. Payroll transactions that are processed for payment prior to supervisory review and approval increases the risk that fraudulent or incorrect payroll disbursements may occur and not be detected timely by management.

Recommendation

We recommend that supervisory staff not involved in the data entry of payroll transactions approve and authorize this before submitting the information to the payroll vendor. We suggest that supervisory accounting staff check batch totals and edit reports.

COUNTY OF YUBA

Management Report – Current Year Comments For the Year June 30, 2008

USE OF MISCELLANEOUS REVENUE ACCOUNT

Condition

We noted that the County's use of the miscellaneous revenue account includes revenue generated from charges for services. During our audit, we noted that the miscellaneous revenue accounts aggregated for County funds were in excess of \$6 million. Miscellaneous revenues account balances were \$626 thousand for the Public Works fund and \$843 thousand and for the Social Services Fund. Additionally, the County is using the miscellaneous revenue account to record revenue in the Workers' Compensation (\$1 million) and Liability Insurance (\$1.7 million) internal service funds.

Effect of Condition

The level of detail for classifying transactions should be sufficiently categorized so as to be meaningful to management in making decisions. When charges for services, a significant revenue source, is combined with miscellaneous revenues, the resulting balance becomes meaningless.

Recommendation

We recommend revenue sources which are the result of providing County services be classified to accounts other than miscellaneous revenues.

COUNTY OF YUBA

Management Report – Current Year Comments For the Year June 30, 2008

UPDATE ROAD INVENTORY RECORDS

Condition

During our audit, we noted that the account balance for inventory reported in the Public Works fund had not changed over several years. Upon further inquiry we were advised that a current year listing of materials and supplies as of June 30, 2008 was not available.

Effect of Condition

The likelihood of assets from the inventory being misappropriated without detection by management is increased when periodical physical accounts are not taken on a regular basis and accounting records are not updated.

Recommendation

We recommend the Public Works department assign staff responsible for completing physical counts of inventory items at least annually at or near June 30th of each year and that this information be submitted to the Auditor-Controller's Office in sufficient time to record adjustments prior to closing the books for the year.

COUNTY OF YUBA

Management Report – Current Year Comments For the Year June 30, 2008

CAPITAL ASSET CAPITALIZATION THRESHOLD

Condition

Currently, the County capitalizes and depreciates all capital assets having an original purchase cost of more than \$500 and an estimated useful life in excess of one year. Such a low threshold creates an administrative burden over the capital asset management system that is costly and difficult to maintain and operate. The accounting process for each asset includes:

1. Identifying the asset
2. Entering it into the capital asset system
3. Assigning a useful life
4. Inventorying it at the end of each fiscal year
5. Depreciating it each year of its useful life
6. Recording its disposition.

Effect of Condition

Current practice has demonstrated that capital asset management systems that attempt to capitalize and depreciate numerous smaller items are costly to maintain and increases the risk of error. The cost of capitalizing and depreciating these assets is greater than the benefit of achieving control and accountability over these items. While it is essential to maintain control over all potentially capitalizable items, there exist much more efficient means than capitalizing and depreciating these assets for financial reporting purposes.

Recommendation

We recommend the County consider increasing the capitalization threshold to no less than \$5,000 for any individual item as recommended by the Government Finance Officer's Association.

COUNTY OF YUBA

Management Report – Current Year Comments For the Year June 30, 2008

CAPITAL ASSET PURCHASING POLICY

Condition

The County does not have a written capital asset purchasing policy and procedures manual that governs the acquisition, use and disposition of the County's capital assets.

Effect of Condition

Internal controls and accounting over capital assets are improved when written policies have been established and communicated. Consistency over accounting for capital assets is achieved when written policies and procedures are in place. Such consistencies decrease the effort required to maintain the fixed asset database.

Recommendation

We recommend the County implement a written capital asset purchasing policy designed to control and account for the County's property and equipment. The County should consider incorporating some or all of the following:

- Establish process for approval of capital assets.
- Differentiate capital assets from maintenance and repair items.
- Establish minimum dollar thresholds for capitalization.
- Set policies for estimating the useful service lives of capital assets.
- Set policies for periodically inventorying capital assets.
- Set policies for disposition or surplusing of capital assets.

COUNTY OF YUBA

Management Report – Current Year Comments For the Year June 30, 2008

CONSISTENT USE OF CAPITAL OUTLAY ACCOUNTS

Condition

The County uses account element 60 to record expenditures for the purpose of capital asset purchases. Since the County has a low capitalization threshold, most activity for the year from this account should reconcile to the County's capital asset additions in its fixed asset management system. During our audit, we compared the capital outlay balances by department to the capital asset additions in the fixed asset management system and we noted immaterial discrepancies. We also noted capital assets capitalized that were recorded to other than the fixed asset account element.

Effect of Condition

The use of a capital outlay account ensures that all capital assets that should be capitalized are identified. Expenditures not meeting the definition of a capital asset should be recorded as maintenance. The capital outlay transactions should be reconciled to the fixed asset additions to ensure that all capital asset items have been included in the County's fixed asset management system.

Recommendation

We recommend that account element 60 be used to only record items meeting the definition of a capital asset and reconcile this account with the additions posted to the County's fixed asset management system.

COUNTY OF YUBA

Management Report – Current Year Comments For the Year June 30, 2008

CAPITAL ASSET RETIREMENTS

Condition

A capital asset processing form is used to record capital asset retirements. The system is updated by indicating a retirement date in the fixed asset software. During the closing process, the County's general ledger accounts are updated by recording the change in capital assets (including the effect of additions) to each fund's fund balance. The ending balance is subtracted from the beginning balance and this difference is adjusted to fund balance where it does not affect any other accounts. Because the change in capital asset balances is netted, there is no way to determine how much of the change is the result of capital asset additions or retirements. The capital asset software does not have a report showing only the retirements for a given period of time.

Effect of Condition

Reports on capital asset retirements provide management with the information necessary to monitor the effectiveness of internal controls. Without these reports, errors or misappropriation can occur during input without being detected by management in a timely manner.

Recommendation

We recommend the County work with the software vendor to create a report of the capital asset retirements within a given period of time. The results of this report should be compared to the information on the capital asset processing form to insure retirements are being accurately recorded.

COUNTY OF YUBA

Management Report – Current Year Comments For the Year June 30, 2008

CAPITAL ASSETS BELONGING TO THE COURTS

Condition

During our review of capital asset balances, we noted that the capital asset balances for the cost of equipment in the General Fund includes the cost of assets belonging to the Courts. These assets do not belong to the County. They should have been transferred to the Courts several years ago when the Court system was separated from the County.

Effect of Condition

By including the cost of the equipment belonging to the Courts, capital asset balances for equipment on the County's financial statements is overstated. The presence of these assets while not material increases the number of assets in the database and the amount of staff time involved to manage and maintain the database. It is not the County's responsibility to account for capital assets belonging to the Courts.

Recommendation

We recommend removing all capital assets where title has been vested to the Courts System.

COUNTY OF YUBA

Management Report – Current Year Comments For the Year June 30, 2008

RECONCILE CAPITAL ASSET RECORDS TO THE GENERAL LEDGER

Condition

During our testing of capital asset transactions and balances, we noted that the County does not reconcile the capital asset purchases recorded in the general ledger to the additions added to the fixed asset database. We also noted that the ending balance of capital assets as contained in the County's fixed asset database did not agree to the final capital asset balances recorded in the County's general ledger at June 30, 2008. Some of these balances were incorrect because of errors made during preparation and input of the journal entry to record the change in capital asset balances.

Effect of Condition

When capital asset purchases are not reconciled to the capital asset listing, errors can occur and not be detected by management on a timely basis.

Recommendation

We recommend the County reconcile the capital asset balances and capital asset purchases in the general ledger to the balances and transactions included in the County's fixed asset database.

COUNTY OF YUBA

Management Report – Current Year Comments For the Year June 30, 2008

STALE DATING OF OUTSTANDING WARRANTS

Condition

During our testing of outstanding warrants at June 30, 2008, we observed that the County's policy is to stale date warrants after 24 months. Our procedures were limited to the County's general warrants and we noted that outstanding warrants were dated as early as January 2006. In California, banking institutes generally are not obligated to honor checks or warrants with issue dates older than six months.

Effect of Condition

Failure to remove stale dated warrants in excess of six months from the County's general ledger increases the cost of tracking old items that have not been redeemed by the payee. Monthly reconciliations are simplified when old outstanding warrants are stale dated and purged from the County's warrant register on a regular basis.

Recommendation

We recommend the County consider changing its policy to stale date warrants after six months.

COUNTY OF YUBA

Status of Prior Management Report Comments As of June 30, 2008

Recommendation	Status/Comment
Year end Closing Procedures We recommend the closing process be documented in a checklist that indicates who will perform each procedure and when completion of each procedure is due.	Not implemented
Journal Entry Process We recommend the County implement the use of a standard journal entry form, available in electronic format and requiring all department personnel to complete it in cases where corrections to accounts are required.	Not implemented
Centralized Purchasing System We recommend the County explore the capabilities of its current accounting system to determine if implementing a centralized purchasing module or system is feasible.	Not implemented
Purchasing Card System We recommend the County explore the use of a purchasing card system to improve the efficiency of your purchasing procedures and to lower the over all costs to process smaller dollar amount purchases.	Implemented
Review of Payroll Input Prior to Processing Paychecks We recommend that supervisory staff not involved in the data entry of payroll transactions approve and authorize this before submitting the information to the payroll vendor.	Not implemented
Use of Miscellaneous Revenue Account We recommend revenue sources which are the result of providing County services be classified to accounts other than miscellaneous revenues.	Not implemented

COUNTY OF YUBA

Status of Prior Management Report Comments As of June 30, 2008

Recommendation	Status/Comment
Update Road Inventory Records We recommend the Public Works department assign staff responsible for completing physical counts of inventory items at least annually at or near June 30 th of each year and that this information be submitted to the Auditor-Controller's Office in sufficient time to record adjustments prior to closing the books for the year.	Not implemented
Capital Asset Capitalization Threshold We recommend the County consider increasing the capitalization threshold to no less than \$5,000 for any individual item as recommended by the Government Finance Officer's Association	Not implemented
Capital Asset Purchasing Policy We recommend the County implement a written capital asset purchasing policy designed to control and account for the County's property and equipment.	Not implemented
Consistent Use of Capital Outlay Accounts We recommend that account element 60 be used to only record items meeting the definition of a capital asset and reconcile this account with the additions posted to the County's fixed asset management system.	Not implemented
Capital Asset Retirements We recommend the County work with the software vendor to create a report of the capital asset retirements within a given period of time	Not implemented
Capital Assets Belonging to the Courts We recommend removing all capital assets where title has been vested to the Courts System.	Not implemented

COUNTY OF YUBA

Status of Prior Management Report Comments As of June 30, 2008

Recommendation	Status/Comment
Reconcile Capital Asset Records to the General Ledger	Not implemented
We recommend the County reconcile the capital asset balances and capital asset purchases in the general ledger to the balances and transactions included in the County's fixed asset database.	
Stale Dating of Outstanding Warrants	Not implemented
We recommend the County consider changing its policy to stale date warrants after six months.	